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SIPDIS
SENSITIVE

DEPT FOR EAP/MTS AND EB/IFD/OMA
TREASURY FOR IA/MALACHY NUGENT
COMMERCE FOR 4430/KELLY
DEPARTMENT PASS FEDERAL RESERVE SAN FRANCISCO FOR CURRAN
DEPARTMENT PASS EXIM BANK
SINGAPORE FOR SBAKER
TOKYO FOR MGREWE
USTR WEISEL, EHLERS

E.O. 12598: N/A
TAGS: EFIN EINV ECON EAGR ID
SUBJECT: STALLED MAYBANK TRANSACTION HIGHLIGHTS LACK OF POLICY
COORDINATION

¶1. (SBU) Summary. The Indonesian Ministry of Finance's Capital Markets Regulatory Agency (BAPEPAM) modified its takeover rules in late June, generating unintended consequences for the regional financial sector. The most visible is the stalled bid by the Malayan Banking Corporation (Maybank) to acquire Bank International Indonesia (BII). The transaction would have allowed Singapore's sovereign wealth fund, Temasek, to conform with Indonesia's single presence policy (SPP), which prohibits a single entity from owning a majority stake in more than one bank by 2010. While there are prudential and market development rationale for both the SPP and the tender offer rules, the implementation of these policies has reinforced the view that financial sector regulations in Indonesia are poorly coordinated and subject to frequent modification. These developments undermine the Indonesian investment climate and progress on ASEAN financial sector integration. End Summary.

Financial Sector Policies Remain Moving Target
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¶2. (SBU) In June, BAPEPAM issued new rules on the acquisition of public companies. The new rules relax regulations for public company acquisition by increasing the level of the purchase which triggers a mandatory tender offer. Acquirers are required to make a tender offer to all stockholders only if they are purchasing 50% or more of the company's shares, or can be shown to have a direct or indirect controlling interest in the firm. The previous trigger level was 25%. The new rules also require the acquirer to ensure that at least 20% of the company's shares are widely held within two years of the acquisition. According to BAPEPAM Chairman Ahmad Fuad Rahmany, the acquisition rules were changed to bring the regulations in line with Indonesia's legal definition of control. Many institutional investors opposed the new regulation as the new rules may allow acquiring firms to take managerial control of a firm without having to make offers to minority shareholders, diluting minority shareholder protection. Market analysts have also questioned the direction of the regulatory change, as the previous rules were broadly in line with international standards.

Malaysian Regulators Block Maybank Transaction
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¶3. (SBU) The new takeover rules prompted Bank Negara Malaysian (BNM), the Malaysian central bank, to block the previously approved acquisition of BII by the (Malaysian) state-owned Maybank,

underscoring the impact of implementing regulatory changes without careful planning or coordination. The Malaysian regulators blocked the transaction over concerns that the requirement to sell as much as 20% of the stock within two years could force Maybank to take significant losses, particularly in light of the agreed price of 4.7 times BII's book value. The Malaysian Ringgit 480 million deposit (US$145 million) that Maybank may forfeit by pulling out of the transaction illustrates the level of concern the Malaysian regulators have over the potential loss. [Note: While companies can be taken private in Indonesia, the fact that Maybank engaged in a bilateral agreement with Temasek to purchase Temasek's BII shares prohibits Maybank from taking BII private, according to BAPEPAM. End Note.]

¶4. (SBU) Maybank reportedly met with BAPEPAM on August 12 to discuss easing the new rules in a move that could reverse BNM's decision. BAPEPAM Chairman Fuad has been widely quoted as stating that BAPEPAM will extend the time frame for compliance with the new regulations under "adverse market conditions," such as a significant drop in a firm's stock price or other capital market problems. Whether an "adverse market" clause will be sufficient to prevent large potential losses at Maybank is yet to be seen. However, the market's perception that BNM's decision was based on second thoughts about the pricing of the deal rather than Indonesia's regulatory change will make it difficult for BAPEPAM to make a more significant exception for Maybank. In a private conversion, BAPEPAM Chairman Fuad put the onus on BNM, noting to the Embassy that BNM had the power to relax Maybank's mark-to-market accounting requirements related to the transaction if they were concerned about accounting losses, suggesting that Indonesia had taken such action in the past.

Inconsistent Policies Undermine Investment,
Regional Integration

¶5. (SBU) Regardless of the outcome of the Maybank transaction, Indonesia's mixed regulatory signals continue to undermine the integrity of Indonesia's regulatory environment and provide disincentives to potential investors. The current owner of BII, Singapore's sovereign wealth fund Temasek, is selling BII in an effort to conform with another relatively recent financial sector regulation, Bank Indonesia's (BI) single presence policy. The single presence requirement prohibits a single entity from owning 25% or more shares of more than one Indonesian banking organization. Temasek also owns Bank Danamon. Policy coordinated between BI and BAPEPAM has been limited in the past, and it is unclear if BI was consulted on the BAPEPAM policy change prior to its announcement. If the Maybank deal fails, Temasek may be forced to merge BII and Bank Danamon or sell BII to the next highest bidder (Bank of China) to comply with the single presence policy. In addition, while BAPEPAM's general reluctance to grant special treatment to Maybank is a positive development from a regulatory standpoint, BAPEPAM suggestion that Malaysia ease accounting rules to accommodate the transaction raises concerns about Indonesia's own commitment to prudential supervisory standards.

¶6. (SBU) The unintended consequences of the new takeover regulation also highlight challenges to regional integration within ASEAN, which the regional block hopes to complete by 2015. The Maybank episode reinforces the market perception that national regulators in ASEAN, in this case BNM, remain closely linked to the business decisions of state-owned banks, rather than arms-length prudential supervisors. The actions and reactions of the Indonesian and Malaysian regulators in this situation also point to a very poor level of communication and coordination among ASEAN authorities.

¶7. (U) This message was coordinated by Embassies Jakarta, Kuala Lumpur, and Singapore.

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